Increasing Fee Income Without Raising Fees

OVER THE PAST 10 YEARS, THE BANKING INDUSTRY has seen a steady decline in fee income associated with checking accounts. Community banks under $10 billion have seen a 32 percent decline and banks over $10 billion have seen a 45 percent decline in fee income when compared to a 2008 baseline. Many institutions are raising fees. Should you?

One option is to start adding minimum balances in order to get additional income from your current customers. Following the lead of big institutions, some community financial institutions have tried to make up fee income by instituting additional account fees, but with disappointing results.

This is not isolated to the banking industry. Other businesses have tried this approach. Several years ago, Starbucks ran a test where they required a minimum purchase in the drive-through to encourage those wanting a $1.85 cup of coffee to come into the store. As you can imagine, the pilot test ended abruptly, less than a month later. What Starbucks knows is when customers come into the store they will spend more; however, creating a minimum-purchase requirement was not the solution. It upset customers and hurt the company's image in those markets.

As community bankers, we need to look through the lens of the prospective consumers. One of the primary reasons people switch banking providers is to eliminate monthly checking account service charges. The majority of consumers still do not want to pay for a checking account. Price matters.

In 2010, prior to the implementation of the *Dodd-Frank* changes related to retail debit cards and overdrafts services, an extremely profitable midsize bank in the Northwest decided to implement a $9-per-month service fee on checking accounts. Its fee income dropped dramatically and attrition went up substantially. In a public statement, the CEO ultimately stated that the bank had made a mistake—but much of the damage was already done. If monthly service charges aren't the answer, then what is?

UNDERSTAND CAPACITY. Understanding capacity is one of the biggest challenges in the banking industry. Financial institutions have very high fixed costs and very low marginal costs. Each branch is an expensive "factory" that is running at 15 percent to 40 percent capacity, 50 percent if you're lucky. The typical community institution averages 1,000 to 1,200 core relationships per branch. The big banks average 3,000 to 5,000 per branch. If you have factories running at 30 percent capacity, your primary objective should be to fill the excess capacity by serving more consumers.

Client data shows marginal expenses—core processor, account servicing, etc.—for the next core checking account are approximately $30 to $50 per year; however, each new core checking account generates approximately $300 to $500 in revenue each year. Excess capacity allows us to look at each new individual as a marginal investment who can spin off multiples in revenue.

While not all customers and members drive the same level of fee income, it is important to create and grow primary financial institute relationships. After analyzing millions of core banking relationships over many years, the data reveals that for 73 percent of account holders the checking account is the

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AFTER ANALYZING MILLIONS OF CORE BANKING RELATIONSHIPS OVER MANY YEARS, THE DATA REVEALS THAT FOR 73 PERCENT OF ACCOUNT HOLDERS THE CHECKING ACCOUNT IS THE FOUNDATION OF THE RELATIONSHIP.

INDUSTRY INSIGHTS

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foundation of the relationship, creating opportunities to provide additional products and services.

UNDERSTAND RISK—REMOVE INEFFECTIVE FILTERS. Most financial institutions use some type of screening service during the account-opening process. Banking professionals need to understand that these services only report *negative* information, which is rarely updated. Client data consistently demonstrates that these systems are not doing what financial institutions think they are doing: reducing fraud. They are, in fact, reducing *opportunities* to grow fee income by turning away customers and members who value overdraft services.

What other filters are you using? Do you require a spouse to be present to open a checking account? If your organization does, you need a better process for adding joint signers after account opening. Credit scoring? Stop it. There is no viable reason to evaluate a credit score prior to opening a checking account. How many forms of ID do you require to establish a relationship? One government issued, unexpired ID should be sufficient as long as consumers can provide their Social Security number (not their Social Security card), physical address (does not need to match the address on the ID) and date of birth. Are you in compliance or well beyond? Think through why your bank is saying *no* today and develop strategies to say *yes* more frequently.

REVIEW OD/NSF SERVICES POLICIES. Provide everyone with up to $100 of overdraft credit at account opening. People who value this service will not wait 30 or 60 days to take advantage of it. Be there when your new customer or member needs you.

We analyzed the subsection of new accounts that had an overdraft in the first 30 days. We found over a seven-month period that banks were seeing a 51 percent closure of accounts when the bank required a 30-day waiting period. We then looked at banks that paid overdrafts early within the first 30 days. There was only a 36 percent attrition rate, meaning 64 percent of the new customers were still active and 79 percent of them continued to utilize overdraft services.

Banking is a business of high fixed costs with low marginal costs for the next core customer or member and high additional revenues. Nearly every financial institution has tremendous capacity. In addition, client data continues to show more accounts equal more profitability and opportunity. The focus should be on growing core relationships and making sound decisions in the process.

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